

2010 JMJ Convertible Promissory Notes

During the year ended December 31, 2010, the Company also issued three additional convertible promissory notes to JMJ Financial, for a total of \$3,000,000 available to receive in cash, for a principal sum of \$3,850,000, which includes an original issue discount of \$850,000. The notes bear a one-time interest charge of 10% on the principal sum. The holder may at its election convert all or part of these notes into shares of the Company's common stock at the conversion rate of the lesser of: (a) \$0.10 per share, or (b) 85% of the average of the three lowest trade prices in the 20 trading days prior to the conversion. During the year ended December 31, 2010, the Company received the entire \$3,000,000 on these additional notes. Of the \$3,850,000 borrowed, the Company converted \$3,562,215 into 76,465,706 shares of common stock. The notes mature on March 30, 2013.

The initial fair value of the embedded conversion option liability associated with the funds received during the year ended December 31, 2010 was valued using the Black-Scholes model, resulting in an initial fair value of \$5,944,408. The assumptions used in the Black-Scholes option pricing model at the dates the funds were received are as follows: (1) dividend yield of 0%; (2) expected volatility of 175-180%, (3) risk-free interest rate of 0.87 – 1.60%, and (4) expected life of 2.47 – 3.00 years.

The value of the conversion option liability underlying the 2010 notes at December 31, 2010 was \$628,919. The Company recognized a gain from the decrease in the fair value of the conversion option liability in the amount of \$3,254,094 during the year ended December 31, 2010, representing the change in fair value during the year.

The following table summarizes all JMJ Financial convertible promissory notes outstanding at December 31, 2010:

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Convertible promissory notes, principal	\$ 287,785
Debt discounts	<u>(285,005)</u>
Net convertible promissory notes	\$ 2,780
Less current portion	<u>(1,585)</u>
Convertible promissory notes, long term	<u>\$ 1,195</u>

As of December 31, 2010 and 2009, respectively, the convertible promissory notes were convertible at the option of the holders into a total of 2,877,850 and 38,898,466 shares, subject to anti-dilution and other customary adjustments. The fair value of the embedded conversion option was \$628,919 and \$2,471,729 at December 31, 2010 and 2009, respectively. The decrease in the fair value of this liability was \$7,778,168 and \$1,490,368 during the years ended December 31, 2010 and 2009, respectively, which was recorded through the results of operations as an adjustment to fair value of derivatives. The assumptions used in the Black-Scholes option pricing model at December 31, 2010 are as follows: (1) dividend yield of 0%; (2) expected volatility of 175%, (3) risk-free interest rate of 0.61%, and (4) expected life of 2.25 years.

During 2010, the debenture holder converted debt valued at \$9,757,190 for 211,916,152 shares of common stock. During 2009, the debenture holder converted debt valued at \$1,269,024 for 14,167,962 shares of common stock.

The Company recorded finance costs in the amount of \$2,669,408 and \$465,370, respectively, in its accompanying consolidated statement of operations for the years ended December 31, 2010 and 2009, representing the excess of the fair value of the conversion option feature over the face value of the JMJ promissory notes.

Interest expense from amortization of debt discounts for the years ended December 31, 2010, 2009 and 2008 was \$6,410,552, \$1,220,220 and \$157,235, respectively. Default interest expense recognized for the years ended December 31, 2010, 2009 and 2008 was \$0, \$84,151 and \$194,420, respectively.